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# **EU JOINT TRANSFER PRICING FORUM**

## **SECRETARIAT DISCUSSION PAPER ON ALTERNATIVE DISPUTE AVOIDANCE AND RESOLUTION PROCEDURES**

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**Centre de Conférences Albert Borschette  
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# 1. Introduction and context

## 1.1. Background

1. Transfer pricing examinations usually cover a number of business years and may lead to large unilateral tax adjustments. To avoid double taxation, the tax authorities of the other Contracting State must agree to make a corresponding adjustment. But even if single taxation is eventually achieved, the costs involved for legal assistance and, in many cases, double payment of taxes are often substantial.
2. Besides the financial factors, an unresolved transfer pricing dispute has other negative effects for the business of the enterprise. It creates uncertainty for the tax years that have not yet been audited, and it can have a negative impact on pending investment decisions.
3. An enterprise that is confronted with transfer pricing adjustments in a country has several choices: (i) it can accept the adjustments, (ii) it can discuss the result with the tax authority, (iii) it can object to the final assessment before the local tax courts, (iv) it can request a Mutual Agreement Procedure (MAP) based on a double tax treaty or, within the EU, (v) it can proceed under the EU Arbitration Convention.<sup>1</sup>
4. A recent favourable innovation in the MAP process has been the use of MAPs in connection with Advance Pricing Agreements (APAs) and other procedures that MNEs can utilize to resolve transfer pricing matters before disputes arise.

## 1.2. EU – The Internal Market

5. So far, the JTPF has looked at ways for speedier and more streamlined dispute resolution procedures in the framework of mutual agreement procedures and arbitration, i.e. after double taxation has occurred. Considering, however, that the overall objectives of any initiative should be the prevention of double taxation and the reduction of the compliance cost, the JTPF in its work programme 2005-2006 (see doc. JTPF/008/REV4/2004/EN of 1<sup>st</sup> December 2004), has agreed to examine also possible preventive measures to avoid double taxation and the acceptability of transfer prices to tax administrations (including APAs).
6. This paper examines alternative procedures to avoid double taxation at the outset and thus reduce the number of traditional dispute resolution and appeals procedures, which are burdensome and time consuming for both tax administrations and taxpayers. The paper also examines supplementary dispute resolution techniques outside the framework of mutual agreement procedures and arbitration. Alternative dispute avoidance and resolution procedures may reduce the likelihood of costly, time consuming and possibly conflicting MAPs and domestic judicial proceedings.

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<sup>1</sup> Some double tax treaties also provide for an arbitration procedure if no mutual agreement is reached between the competent authorities, but they do not provide for mandatory arbitration.

7. An issue of great importance for the concrete solving of cross-border transfer pricing disputes is, in any case, the promotion of administrative co-operation between national tax authorities.

### ***1.3. OECD – Joint Working Group on Dispute Resolution***

8. To take forward the work on improving dispute resolution, the OECD created a joint working group composed of Working Party 1 (Double Tax Conventions) and Working Party 6 (Transfer Pricing) delegates from OECD Member States' tax administrations. The OECD on 27 July 2004 released for public comment a Progress Report on "Improving the Process for Resolving International Tax Disputes" . The report describes different kinds of proposals covering both operational and substantive issues for improving dispute resolution. The report states that the mutual agreement procedure can sometimes take a long time and use a considerable amount of taxpayer and tax administration resources. As such results are unsatisfactory to all concerned, a number of Supplementary Dispute Resolution ("SDR") techniques are, therefore, being considered in the report to deal with such situations, ranging from an advisory opinion to a more formal arbitration process.

### ***1.4. PATA – Guidance on Mutual Agreement Procedures and Bilateral Advance Pricing Arrangements***

9. The Pacific Association of Tax Administrators (PATA) on 25 June 2004 issued internal operational guidance covering mutual agreement procedures (MAPs) and bilateral advance pricing arrangements (BAPAs) amongst its member countries.
10. The guidance was issued in two documents. The first document is entitled "MAP Operational Guidance for Member Countries of the Pacific Association of Tax Administrators" and is intended to facilitate and support resolution of MAP cases amongst PATA member countries as well as to ensure consistent and timely treatment of such cases. The second document is entitled "BAPA Operational Guidance for Member Countries of the Pacific Association of Tax Administrators" and is intended to establish a common approach for treating taxpayers in a fair and consistent manner when seeking BAPAs, provide a working framework that enables the smooth and timely completion of BAPAs and encourage and facilitate the use of BAPAs amongst PATA member countries. The purpose of releasing these internal working documents is to increase the level of transparency in the MAP and BAPA processes within PATA member countries.
11. The main objectives of the PATA Guidance are:
  - to establish a common approach for treating taxpayers in a fair and consistent manner when seeking a bilateral or multilateral APA;
  - to provide a working framework that enables the smooth and timely completion of APAs; and
  - to encourage and facilitate the use of APAs among PATA Members.

## **2. Possible forms of alternative dispute avoidance and resolution procedures**

### **2.1. Advance Pricing Agreements (APAs)**

#### *a) Definition and Functioning of APAs*

12. One possibility to overcome the problem of uncertainty of transfer pricing both for business and national tax administrations are APAs, which for the taxpayer are a means to request a binding transfer pricing ruling from the tax administration(s) on the treatment of future transactions involving transfer prices. The disadvantage is that so far they can usually only be obtained via a lengthy and costly procedure, both for taxpayers and tax administrations, which makes them generally useful only for very important cases. However, such disadvantage must be compared to the length and the cost of an audit and an MAP and/or litigation.
13. An APA is an arrangement that determines, in advance of controlled transactions, an appropriate set of criteria (e.g. method, comparables and appropriate adjustments thereto, critical assumptions as to future events) for the determination of the transfer pricing for those transactions over a fixed period of time.
14. An APA is formally initiated by a taxpayer and requires negotiations between the taxpayer, one or more associated enterprises, and one or more tax administrations. APAs are intended to supplement the traditional administrative, judicial, and treaty mechanisms for resolving transfer pricing issues. They may be most useful when traditional mechanisms fail or are difficult to apply.
15. APAs can be unilateral (an agreement between the taxpayer and one tax administration), bilateral (an agreement involving the taxpayer and two countries where the taxpayer's affiliates reside) or multilateral (situations where multiple tax jurisdictions are part of an APA).<sup>2</sup> The arrangements involving more than one country are usually covered under the MAP of the countries involved.
16. Some countries allow for unilateral arrangements where the tax administration and the taxpayer in its jurisdiction establish an arrangement without the involvement of other interested tax administrations. However, a unilateral APA may affect the tax liability of associated enterprises in other tax jurisdictions. Where unilateral APAs are permitted, the competent authorities of other interested jurisdictions should be informed about the procedure as early as possible to determine whether they are willing and able to consider a bilateral arrangement under the mutual agreement procedure.
17. Because of concerns over double taxation, most countries prefer bilateral or multilateral APAs (i.e. an arrangement in which two or more countries concur), and indeed some

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<sup>2</sup> For instance, a multilateral APA was signed on 8 April 2004 by Airbus Industries and the tax administrations of France, Germany, the United Kingdom and Spain.

countries will not grant a unilateral APA (i.e. an arrangement between the taxpayer and one tax administration) to taxpayers in their jurisdiction. However, in many countries unilateral APAs are more numerous than bilateral/multilateral APAs, not least because unilateral APAs can be concluded faster and less costly. The bilateral (or multilateral) approach is far more likely to ensure that the arrangements will reduce the risk of double taxation, will be equitable to all tax administrations and taxpayers involved, and will provide greater certainty to the taxpayers concerned. It is also the case in some countries that domestic provisions do not permit the tax administrations to enter into binding agreements directly with the taxpayers, so that APAs can be concluded with the competent authority of a treaty partner only under the mutual agreement procedure.

***Question 1:*** *Tax Administration Members are invited to inform the Forum whether their country provides for (a) unilateral and/or (b) bilateral/multilateral APAs.*

18. APAs, including unilateral ones, differ in some ways from more traditional private rulings that some tax administrations issue to taxpayers. An APA generally deals with factual issues, whereas more traditional private rulings tend to be limited to addressing questions of a legal nature based on facts presented by a taxpayer. The facts underlying a private ruling request may not be questioned by the tax administration, whereas in an APA the facts are likely to be thoroughly analysed and investigated. In addition, an APA usually covers several transactions, several types of transactions on a continuing basis, or all of a taxpayer's international transactions for a given period of time. In contrast, a private ruling request usually is binding only for a particular transaction.
19. An APA may cover all of the transfer pricing issues of a taxpayer (as is preferred by some countries) or may provide a flexibility to the taxpayer to limit the APA request to specified affiliates and intercompany transactions. An APA would apply to future years and transactions and the actual term would depend on the industry, products or transactions involved. The associated enterprises may limit their request to specified prospective tax years. An APA can provide an opportunity to apply the agreed transfer pricing methodology to resolve similar transfer pricing issues in open prior years. However, this application would require the agreement of the tax administration, the taxpayer, and, where appropriate, the treaty partner.

*b) Advantages of APAs*

20. An APA programme can assist taxpayers by eliminating uncertainty through enhancing the predictability of tax treatment in international transactions. Provided the critical assumptions are met, an APA can provide the taxpayers involved with certainty in the tax treatment of the transfer pricing issues covered by the APA for a specified period of time. In some cases, an APA may also provide an option to extend the period of time to which it applies. When the term of an APA expires, the opportunity may also exist for the relevant tax administrations and taxpayers to renegotiate the APA. Because of the certainty provided by an APA, a

taxpayer may be in a better position to predict its tax liabilities, thereby providing a tax environment that is favourable for investment.

21. Typically, associated enterprises are allowed to participate in the process of obtaining an APA, by presenting the case to and negotiating with the tax administrations concerned, providing necessary information, and reaching agreement on the transfer pricing issues. From the associated enterprises' perspective, this ability to participate may be seen as an advantage over the conventional mutual agreement procedure.
22. Due to the taxpayer participation, APAs can provide an opportunity for both tax administrations and taxpayers to consult and cooperate in a non-adversarial spirit and environment. The opportunity to discuss complex tax issues in a less confrontational atmosphere than in a transfer pricing examination can stimulate a free flow of information among all parties involved for the purpose of coming to a legally correct and practicably workable result. The non-adversarial environment may also result in a more objective review of the submitted data and information than may occur in a more adversarial context (e.g. litigation). The close consultation and cooperation required between the tax administrations in an APA program also leads to closer relations with treaty partners on transfer pricing issues.
23. An APA may prevent costly and time-consuming examinations and litigation of major transfer pricing issues for taxpayers and tax administrations. Once an APA has been agreed, less resources may be needed for subsequent examination of the taxpayer's return, because more information is known about the taxpayer. It may still be difficult, however, to monitor the application of the arrangement. The APA process itself may also present time savings for both taxpayers and tax administrations over the time that would be spent in a conventional tax examination, although in the aggregate there may be no net time savings, for example, where the existence of an APA may not directly affect the amount of resources devoted to compliance.
24. Bilateral and multilateral APAs substantially reduce or eliminate the possibility of juridical or economic double or non taxation since all the relevant countries participate. By contrast, unilateral APAs do not provide certainty in the reduction of double taxation because tax administrations affected by the transactions covered by the APA may consider that the methodology adopted does not give a result consistent with the arm's length principle. In addition, bilateral and multilateral APAs can enhance the mutual agreement procedure by significantly reducing the time needed to reach an agreement since competent authorities are dealing with current data as opposed to prior year data that may be difficult and time-consuming to produce.
25. The disclosure and information aspects of an APA programme as well as the cooperative attitude under which an APA can be negotiated may assist tax administrations in gaining insight into complex international transactions undertaken by MNEs. An APA programme can improve knowledge and understanding of highly technical and factual circumstances in areas such as global trading and the tax issues involved. The development of specialist skills that focus on particular industries or specific types of transactions will enable tax administrations to give better service to other taxpayers in similar circumstances. Through an

APA programme tax administrations have access to useful industry data and analysis of pricing methodologies in a cooperative environment.

*c) Disadvantages of APAs*

*(i) Unilateral vs. bilateral/multilateral APAs*

26. Unilateral APAs may present significant problems for tax administrations and taxpayers alike. From the point of view of other tax administrations, problems may arise because they may disagree with the APA's conclusions. From the point of view of the associated enterprises involved, one problem is the possible effect on the behaviour of the associated enterprises. Unlike bilateral or multilateral APAs, the use of unilateral APAs may not lead to an increased level of certainty for the taxpayer involved and a reduction in economic or juridical double taxation for the MNE group. If the taxpayer accepts an arrangement that over-allocates income to the country making the APA in order to avoid lengthy and expensive transfer pricing enquiries or excessive penalties, the administrative burden shifts from the country providing the APA to other tax jurisdictions.
27. Another problem with a unilateral APA is the issue of corresponding adjustments. The flexibility of an APA may lead the taxpayer and the related party to accommodate their pricing to the range of permissible pricing in the APA. In a unilateral APA, it is critical that this flexibility preserve the arm's length principle since a foreign competent authority is not likely to allow a corresponding adjustment arising out of an APA that is inconsistent, in its view, with the arm's length principle.
28. On the other hand, there are cases where unilateral APAs may be helpful or even the only possibility. For example, in countries, e.g. Italy, where only unilateral APAs are available, or in cases where too many countries are involved, a unilateral APA may be the only pragmatic solution. The same may be true for SMEs and in cases where only a small amount of tax is at stake or where the tax issue is not difficult and does not require the heavier process of a bilateral or multilateral APA.

*(ii) Specific disadvantages for tax administrations*

29. An APA program may initially place a strain on transfer pricing audit resources, as tax administrations will generally have to divert resources earmarked for other purposes (e.g. examination, advising, litigation, etc.) to the APA programme. Demands may be made on the resources of a tax administration by taxpayers seeking the earliest possible conclusion to an APA request, keeping in mind their business objectives and time scales, and the APA programme as a whole will tend to be led by the demands of the business community. These demands may not coincide with the resource planning of the tax administrations, thereby making it difficult to process efficiently both the APAs and other equally important work. Renewing an APA, however, is likely to be less time-consuming than the process of initiating an APA. The renewal process may focus on updating and adjusting facts, business and

economic criteria, and computations. In the case of bilateral arrangements, the agreement of the competent authorities of both Contracting States is to be obtained on the renewal of an APA to avoid double taxation (or non-taxation).

30. Concerns have also been expressed that, because of the nature of the APA procedure, it will interest taxpayers with a good voluntary compliance history. Experience in some countries has shown that, most often, taxpayers which would be interested in APAs are very large corporations which would be audited on a regular basis, with their pricing methodology then being examined in any event. The difference in the examination conducted of their transfer pricing would be one of timing rather than extent. There are also differences in terms of climate and penalties. As well, it has not been demonstrated that APAs will be of interest solely or principally to such taxpayers. Indeed, there are some early indications that taxpayers, having experienced difficulty with tax administrations on transfer pricing issues and not wishing these difficulties to continue, are often interested in applying for an APA. There is then a serious danger of audit resources and expertise being diverted to these taxpayers and away from the investigation of less compliant taxpayers, where these resources could be better deployed in reducing the risk of losing tax revenue. However, as mentioned above, MNEs are audited on a regular basis, so for them, there is no diversion of resources. The balance of compliance resources may be particularly difficult to achieve since an APA programme tends to require highly experienced and often specialised staff. Requests for APAs may be concentrated in particular areas or sectors, e.g. global trading, and this can overstretch the specialist resources already allocated to those areas by the authorities. Tax administrations require time to train experts in specialist fields in order to meet unforeseeable demands from taxpayers for APAs in those areas.

*(iii) Specific disadvantages for taxpayers*

31. An APA might seek more detailed industry and taxpayer specific information than would be requested in a transfer pricing examination. In principle, this should not be the case and the documentation required for an APA should not be more onerous than for an examination, except for the fact that in an APA the tax administration will need to have details of predictions and the basis for those predictions, which may not be central issues in a transfer pricing examination that focuses on completed transactions. In fact, an APA should seek to limit the documentation, as discussed above, and focus the documentation more closely on the issues in light of the taxpayer's business practices. Tax administrations need to recognize that :
- a) publicly available information on competitors and comparables is limited;
  - b) not all taxpayers have the capacity to undertake in-depth market analyses; and
  - c) only parent companies may be knowledgeable about group pricing policies.
32. Another possible concern is that an APA may allow the tax administration to make a closer study of the transactions at issue than would occur in the context of a transfer pricing examination, depending on the facts and circumstances. The taxpayer must provide detailed information relating to its transfer pricing and satisfy any other requirements imposed for the



verification of compliance with the terms and conditions of the APA. At the same time, the taxpayer is not sheltered from normal and routine examinations by the tax administration on other issues. An APA also does not shelter a taxpayer from examination of its transfer pricing activities. The taxpayer may still have to establish that it has complied in good faith with the terms and conditions of the APA, that the material representations in the APA remain valid, that the supporting data used in applying the methodology were correct, that the critical assumptions underlying the APA are still valid and are applied consistently, and that the methodology is applied consistently.

33. Problems could also develop if tax administrations misuse information obtained in an APA in their examination practices. If the taxpayer withdraws from its APA request or if the taxpayer's application is rejected after consideration of all of the facts, any nonfactual information provided by the taxpayer in connection with the APA request, such as settlement offers, reasoning, opinions, and judgments, cannot be treated as relevant in any respect to the examination. In addition, the fact that a taxpayer has applied unsuccessfully for an APA should not be taken into account by the tax administration in determining whether to commence an examination of that taxpayer.
34. An APA program cannot be used by all taxpayers because the procedure can be expensive and time-consuming and small taxpayers generally may not be able to afford it. This is especially true if independent experts are involved. APAs may therefore only assist in resolving mainly large transfer pricing cases. In addition, the resource implications of an APA program may limit the number of requests a tax administration can entertain. In evaluating APAs, tax administrations can alleviate these potential problems by ensuring that the level of inquiry is adjusted to the size of the international transactions involved.

**Question 2:** *Do Forum Members agree with the above analysis of the possible pros and cons of APAs?*

**Question 3:** *Do Forum Members agree that in light of the advantages of APAs for both tax administrations and taxpayers all Member States should provide at least for bilateral/multilateral APAs (at least with other EU Member States)?*

*d) The OECD Guidelines on APAs*

35. In 1999 the OECD has issued Guidelines on the use of APAs within the framework of the mutual agreement procedure of the double tax treaties (see Annex). The OECD is trying actively to promote the use of APAs as a mechanism to reduce tax conflicts between tax administrations and taxpayers in the application of the arm's length principle.

e) *EU-wide standardised APAs (pan-European APA model)*

36. In recent years, several EU Member States have introduced specific regulations on APAs, for example Spain in 1996, France in 1999, the UK in 1999, the Netherlands in 2001 and Belgium in 2002. In France, the Finance Amendment Bill 2005 contains provisions instituting a formally legislated APA procedure to replace the current informal procedure.
37. The different sets of rules governing the various APA procedures in Member States are time consuming and burdensome for businesses. Because bilateral and multilateral APAs require two or more tax administrations to agree on the transfer pricing approach, it is much easier if the various jurisdictions use a similar approach. In the absence of a common approach, it can sometimes be extraordinarily difficult for the tax administrations to reach agreement. Differences in the APA approach can sometimes lead to contentious negotiations that ultimately may fail to produce an APA and that may be costly for all involved and produce potential double taxation. Common guidelines providing clarity for both taxpayers and tax administrations could be a remedy.

***Question 4:*** *Would the Forum be prepared to examine the possibilities of a common approach on APAs, i.e. creating a EU Model APA, as a means to avoid double taxation resulting from transfer pricing adjustments?*

38. In case the Forum wishes to deepen its analysis on APAs, the following issues may be worthwhile for further examination:
- Tax issues to be covered by an APA;
  - Number of years to be covered by an APA;
  - Procedures for possible prolongation;
  - Application of APAs to open prior years, e.g. tax years under examination/tax audit;
  - Binding effects on tax administrations and taxpayers;
  - Fees; and
  - Publication.

**2.2. Facilitating access to APAs for SMEs ("Mini-APAs")**

39. The complexity and cost of the APA procedure discourage many SMEs from using this procedure. To alleviate this problem specific procedures for SMEs could be applied, such as:
- streamlining the requests made by the tax administration to assess the company's transfer pricing policy by, for example, reducing the documentation requirements or the requests relating to comparables; and

- increased support from the tax administration in the creation and review of the APA application by the company

***Question 5:*** Does the Forum think it is worthwhile considering ways of facilitating access to APAs for SMEs ("Mini-APAs")?

### **2.3. Simultaneous tax examinations**

40. A simultaneous tax examination, as defined in Part A of the OECD Model Agreement for the Undertaking of Simultaneous Tax Examinations, means an "arrangement between two or more parties to examine simultaneously and independently, each on its own territory, the tax affairs of (a) taxpayer(s) in which they have a common or related interest with a view to exchanging any relevant information which they so obtain".
41. Cooperation and mutual assistance between tax administrations in the EU with regard to transfer pricing has been intensified in recent years. This enhanced cooperation has been made possible by means of different mechanisms such as, for example, the exchange of information and, to a lesser degree, simultaneous tax examinations and the visits of tax auditors of a Member State in another Member State. In this context it is worth mentioning, that EC Directive 77/799/EC on the exchange of information in direct and indirect taxes has recently been modified in order to implement a procedure for "simultaneous tax inspections" (Article 8.3 of Directive 2004/56/EC).

***Question 6:*** Would the Forum be prepared to examine the possibilities and a common approach on simultaneous tax examinations as a means to avoid double taxation resulting from transfer pricing adjustments?

### **2.4. Voluntary or mandatory prior consultation**

42. The European Commission working paper "Company taxation in the internal market" of 23 October 2001 suggests as a means to improve the practical application of the EU Arbitration Convention, among other things, a framework for prior agreement or consultation before tax administrations make transfer pricing adjustments.
43. Paragraph 29 a) of the Commentary to Article 25 OECD Model Tax Convention provides that tax administrations should notify taxpayers as soon as possible of their intention to make a transfer pricing adjustment, since it is particularly useful to ensure as early and as full contacts as possible on all relevant tax matters between tax administrations and taxpayers within the same jurisdiction and, across national frontiers, between the associated enterprises and the other tax administrations concerned.

44. Similarly, Article 5 of the Arbitration Convention provides:

Where a Contracting State intends to adjust the profits of an enterprise in accordance with the principles set out in Article 4, it shall inform the enterprise of the intended action in due time and give it the opportunity to inform the other enterprise so as to give that other enterprise the opportunity to inform in turn the other Contracting State. However, the Contracting State providing such information shall not be prevented from making the proposed adjustment. If after such information has been given the two enterprises and the other Contracting State agree to the adjustment, Articles 6 and 7 shall not apply.

45. The Arbitration Convention (like bilateral double tax treaties) does, however, not oblige the tax administration of a Member State to agree in advance on an appropriate transfer price with the tax administration of the affiliated company before a transfer pricing adjustment is made. This procedure would solve most of the business concerns; i.e. the double taxation itself, the costs of temporarily having to finance the same tax burden twice, business costs of seeking double tax relief etc. However, tax administrations might argue that such a rule would increase their administrative burden, lead to more aggressive tax planning, and require substantial extension of the periods where tax returns are open etc. Since both concerns are valid, the basic idea of prior approval or the agreement on a less stringent and voluntary consultation procedure should therefore be considered in more detail.

46. Under such a prior consultation procedure, the tax administration of the country where the primary adjustment is to be made, would be required to consult the tax administrations of the other Member States concerned in advance regarding this adjustment. This process would give the various tax administrations the possibility of entering into discussions at an early stage and foster more cooperation between the tax administrations.

47. However, this procedure would not guarantee that the double taxation issue would be resolved in advance, because it only implies a consultation and not a prior approval of the tax administrations of the other Member States concerned. Introducing a prior consultation process in the auditing practice related to transfer pricing could, nevertheless, be a more pragmatic way to resolve, or rather avoid, double taxation problems under the Arbitration Convention.

48. The current order of process being tax examination, reassessment and ultimately MAP (or appeals procedure) would be replaced with the following process: tax examination followed by a mutually agreed reassessment (corresponding to the result of the prior consultation or MAP). Such a process would lift the responsibility for settling transfer pricing disputes within the EU from the business level to the level where the claims are made, i.e. at the level of Member States. As a result, the reassessment would be made at approximately the same time as the corresponding adjustment in the other Contracting State.

**Question 7:** *Would the Forum be prepared to examine the scope for voluntary or mandatory prior consultation?*

**Question 8:** *Would the Forum be prepared to examine ways of changing the current process of making transfer pricing adjustments as outlined in paragraph 48 above?*

## **2.5. Expert opinion ("mediation")**

49. Whereas the examination of the previous issues should result in the avoidance of double taxation, in practice it might be difficult to achieve. It is therefore imperative to have appropriate dispute settlement mechanisms that relieve double taxation as quickly and efficiently and in as many cases as possible, and with the lowest possible costs for business and tax administrations. Obtaining an expert opinion or mediation may be a possible means for speedier and more streamlined dispute resolution procedures.

50. The current Commentary to Article 25 (paragraph 46) of the OECD Model Tax Convention on Income and on Capital discusses the possibility of competent authorities to obtain an “advisory opinion” from an impartial expert to help them reach a decision. In addition, the Commentary (paragraph 47) foresees the possibility of the parties obtaining an “opinion” on the “correct understanding” of a treaty provision from the OECD's Committee on Fiscal Affairs. Further, paragraph 4 of Article 25 of the OECD Model Tax Convention and paragraphs 4 and 41 of the Commentary on that Article foresee the possible formation of a “joint commission” to deal with some issues. Another possibility is to have a third party evaluate the strengths and weaknesses of positions taken by the competent authorities. These techniques are forms of “mediation” in which a third party assists the competent authorities in reaching a decision but generally does not have any independent decision making power.

**Question 9:** *Would the Forum be prepared to examine the possibilities of obtaining an expert opinion ("mediation") in the context of the MAP?*

**Question 10:** *Do Forum Members think that this paper sufficiently covers the issues to be addressed or are there any other issues the Forum wishes to discuss?*

## Annex

### OECD GUIDELINES FOR CONDUCTING ADVANCE PRICING ARRANGEMENTS UNDER THE MUTUAL AGREEMENT PROCEDURE ("MAP APAs")

#### A. Background

##### i) Introduction

1. Advance Pricing Arrangements ("APAs") are the subject of extensive discussion in the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD 1995) (hereafter referred to as the "Transfer Pricing Guidelines") at Chapter IV, Section F. The development of working arrangements between competent authorities is considered at paragraph 4.165:

“Between those countries that use APAs, greater uniformity in APA practices could be beneficial to both tax administrations and taxpayers. Accordingly, the tax administrations of such countries may wish to consider working agreements with the competent authorities for the undertaking of APAs. These agreements may set forth general guidelines and understandings for the reaching of mutual agreement in cases where a taxpayer has requested an APA involving transfer pricing issues.” It should be noted that the use of the term “agreement” in the above quotation is not intended to give any status to such procedural arrangements above that provided for by the Mutual Agreement Article of the OECD Model Tax Convention. Additionally, the Committee on Fiscal Affairs stated at paragraph 4.161 of the Transfer Pricing Guidelines that it intended “to monitor carefully any expanded use of APAs and to promote greater consistency in practice amongst those countries that choose to use them.”

2. This Annex follows up on the above recommendations. The objective is to improve the consistency of application of APAs by providing guidance to tax administrations on how to conduct mutual agreement procedures involving APAs. Although the focus of the Annex is on the role of tax administrations, the opportunity is taken to discuss how best the taxpayer can contribute to the process. This guidance is intended for use by those countries -- both OECD Members and non-members -- that wish to use APAs.

##### ii) Definition of an APA

3. Many jurisdictions have had, for some time, procedures (e.g. rulings) enabling the taxpayer to obtain some degree of certainty regarding how the law will be applied in a given set of circumstances. The legal consequences of the proposed action are determined in advance, based on assumptions about the factual basis. The validity of this determination is dependent upon the assumptions being supported by the facts when the actual transactions take place. The term APA refers to a procedural arrangement between a taxpayer or taxpayers and a tax administration intended to resolve potential transfer pricing disputes in advance. The APA differs from the classic ruling procedure, in that it requires the detailed review and to the extent appropriate, verification of the factual assumptions on which the determination of legal consequences is based, before any such determination can be made. Further, the APA provides for a continual monitoring of whether the factual assumptions remain valid throughout the course of the APA period.

4. An APA is defined in the first sentence of paragraph 4.124 of the Transfer Pricing Guidelines as “an arrangement that determines, in advance (emphasis added) of controlled transactions, an appropriate set of criteria (e.g. method, comparables and appropriate adjustments thereto, critical assumptions as to future events) for the determination of the transfer pricing for those transactions over a fixed period of time.” It is also stated in paragraph 4.132 that “The concept of APAs also may be useful in resolving issues raised under Article 7 of the OECD Model Tax Convention relating to allocation problems, permanent establishments, and branch operations.”

5. In the Transfer Pricing Guidelines (see paragraph 4.130) the arrangements solely between a taxpayer or taxpayers and a tax administration are referred to as “unilateral APAs”. The Transfer Pricing Guidelines encourage bilateral APAs and recommend at paragraph 4.163 that “Wherever possible, an APA should be concluded on a bilateral or multilateral basis between competent authorities through the mutual agreement procedure of the relevant treaty.” A bilateral APA is based on a single mutual agreement between the competent authorities of two tax administrations under the relevant treaty. A multilateral APA is a term used to describe a situation where there is more than one bilateral mutual agreement.

6. Although, commonly an APA will cover cross-border transactions involving more than one taxpayer and legal enterprise, i.e. between members of a Multinational Enterprise (MNE) group, it is also possible for an APA to apply to only one taxpayer and legal enterprise. For example, consider an enterprise in Country A that trades through branches in Countries B, C and D. In order to have certainty that double taxation will not occur, countries A, B, C and D will need to share a common understanding of the measure of profits to be attributed to each jurisdiction in respect of that trading activity under Article 7 of the OECD Model Tax Convention. This certainty could be achieved by the negotiation of a series of separate, but mutually consistent, bilateral mutual agreements, i.e. between A and B, A and C and A and D. The existence of multiple bilateral mutual agreements raises a number of special issues and these are discussed further in Section B, paragraphs 21-27 of this Annex.

7. It is important to distinguish the different types of APAs and so the bilateral or multilateral APAs, which are the main subject of this Annex, are hereafter referred to as “MAP APAs”. The APAs that do not involve a mutual agreement negotiation are referred to as “unilateral APAs”. The generic term “APA” is used where the feature to be discussed applies to both types of APA. It should be noted that, in the vast majority of cases a bilateral APA will be concluded under the mutual agreement procedure of a double tax convention. However, in some cases where a bilateral APA has been sought and the treaty is not appropriate, or where a treaty is not applicable, the competent authorities of some countries may nevertheless conclude an arrangement using the executive power conferred on the heads of tax authorities. The term MAP APA should be interpreted, with the necessary adaptations, as including such exceptional agreements.

8. The focus of this Annex is on providing guidance to enable tax authorities to resolve disputes through the Mutual Agreement Procedure, thereby helping to eliminate the risk of potential double taxation and providing the taxpayer with reasonable certainty of tax treatment. However, it should be noted that there are other mechanisms for achieving the same goals which are not discussed in this Annex.

### iii) Objectives of the APA process

9. It has been the experience of a number of countries that the resolution of transfer pricing disputes by traditional audit or examination techniques has often proved very difficult and also costly for taxpayers and tax authorities both in terms of time and resources. Such techniques inevitably examine transfer prices (and the surrounding conditions) some time after they were set and there can be genuine difficulties in obtaining sufficient information to evaluate properly whether arm’s length prices were used at the time they were set. These difficulties led in part to the development of the APA process as an alternative way of solving transfer pricing issues in some cases in order to avoid some of the problems described above. The objectives of an APA process are to facilitate principled, practical and co-operative negotiations, to resolve transfer pricing issues expeditiously and prospectively, to use the resources of the taxpayer and the tax administration more efficiently, and to provide a measure of predictability for the taxpayer.

10. To be successful, the process should be administered in a nonadversarial, efficient and practical fashion and requires the co-operation of all the participating parties. It is intended to supplement, rather than replace, the traditional administrative, judicial, and treaty mechanisms for resolving transfer pricing

issues. Consideration of an APA may be most appropriate when the methodology for applying the arm's length principle gives rise to significant questions of reliability and accuracy, or when the specific circumstances of the transfer pricing issues being considered are unusually complex.

11. One of the key objectives of the MAP APA process is the elimination of potential double taxation. Unilateral APAs give rise to considerable concerns in this area, which is why "most countries prefer bilateral or multilateral APAs" (paragraph 4.131 of the Transfer Pricing Guidelines). However, some kind of confirmation or agreement between the taxpayer and the tax administration is necessary in order to give effect to the MAP APA in each of the participating jurisdictions. The exact form of such confirmation or agreement depends on the domestic procedures in each jurisdiction (discussed in more detail at paragraphs 65-66 below). Such a confirmation or agreement also provides a mechanism to ensure that the taxpayer complies with the terms and conditions of the MAP APA on which this confirmation or agreement is based.

12. Further, in order to meet the objectives described in this section, the MAP APA process needs to be conducted in a neutral manner. In particular, the process should be neutral as regards the residence of the taxpayer, the jurisdiction in which the request for the MAP APA was initiated, the audit or examination status of the taxpayer and the selection of taxpayers in general for audit or examination. The guidance at paragraph 4.157 of the Transfer Pricing Guidelines on possible misuse by tax administrations in their examination practices of information obtained in the APA process should also be borne in mind. The guidance given in this Annex is intended to assist in attaining the objectives described in this section.

## B. Eligibility for a MAP APA

### i) Treaty issues

13. The first question that arises is whether it is possible for there to be an APA. The eligibility of a taxpayer to apply for a unilateral APA will be determined by the specific domestic requirements of the relevant tax administration. MAP APAs are governed by the mutual agreement procedure of the applicable double tax agreement, Article 25 of the OECD Model Tax Convention, and are administered at the discretion of the relevant tax administrations.

14. In some cases the taxpayer will only request a unilateral APA. The reasons for the taxpayer not requesting a MAP APA should be explored. Following the guidance given by the Transfer Pricing Guidelines at paragraph 4.163 that "wherever possible, an APA should be concluded on a bilateral or multilateral basis", the tax authorities should encourage the taxpayer to request a MAP APA if the circumstances so warrant. Some countries if they determine that another tax administration should be involved may refuse to enter into unilateral negotiations with the taxpayer, even though the taxpayer still insists on a unilateral approach.

15. The negotiation of a MAP APA requires the consent of the relevant competent authorities. In some cases, the taxpayer will take the initiative by making simultaneous requests to the affected competent authorities. In other cases the taxpayer may file a request with one jurisdiction under the relevant domestic procedure and ask it to contact the other affected jurisdiction(s) to see if a MAP APA is possible. Consequently, as soon as is administratively practicable, the competent authority in that jurisdiction should notify the relevant tax treaty partner(s) to determine whether they want to participate. The other tax administration should respond to the invitation as quickly as practicable, bearing in mind the need to have sufficient time to evaluate whether their participation is possible or feasible.

16. However, Article 25 does not oblige the competent authorities to enter into MAP APAs at the request of the taxpayer. The willingness to enter into MAP APAs will depend on the particular policy of a country and how it interprets the Mutual Agreement Article of its bilateral treaties. Some competent authorities



will only consider such an agreement for cases that require the resolution of “difficulties or doubts arising as to the interpretation or application of the Convention”. The desire of the taxpayer for certainty of treatment is therefore not, in isolation, sufficient to pass the above threshold. Other competent authorities apply a less restrictive threshold for entering into MAP APAs, based on their view that the MAP APA process should be encouraged. Additionally, the taxpayer must qualify for the benefit of a particular treaty (e.g. by qualifying as a resident of one of the Contracting States) and must satisfy any other criteria contained in the Mutual Agreement Article.

ii) Other factors

17. The fact that a taxpayer may be under audit or examination should not prevent the taxpayer from requesting a MAP APA in respect of prospective transactions. The audit or examination and the mutual agreement procedure are separate processes and generally can be resolved separately. Audit or examination activities would not normally be suspended by a tax administration whilst the MAP APA is being considered, unless it is agreed by all parties that the audit or examination should be held in abeyance because the obtaining of the MAP APA would assist with the completion of the audit or examination. Nevertheless, the treatment of the transactions being audited or examined may be informed by the methodology agreed to be applied prospectively under the MAP APA, provided that the facts and circumstances surrounding the transaction under audit or examination are comparable with those relating to the prospective transactions. This issue is discussed further in paragraph 69 below.

18. The ability to conclude a MAP APA is predicated on full co-operation by the taxpayer. The taxpayer and any associated enterprises should: (i) provide their full co-operation in assisting the tax administrations with the evaluation of their proposal; and (ii) provide, upon request, any additional information necessary for that evaluation, for example, details of their transfer pricing transactions, business arrangements, forecasts and business plans, and financial performance. It is desirable that this commitment from the taxpayer be sought before commencing the MAP APA process.

19. In some cases the freedom of one or both competent authorities to agree to a MAP APA may be limited, for example by a legally binding decision affecting issues subject to the APA proposals. In such circumstances, as the MAP APA process is by definition consensual, it is within the discretion of the affected competent authorities (subject to the domestic laws and policies of each jurisdiction) whether to engage in MAP APA discussions. For example, a competent authority may decline to enter into discussions if it determines that such a limitation on the position of the other competent authority unacceptably reduces the likelihood of mutual agreement. However, it is likely that in many cases MAP APA discussions would be viewed as desirable even though the flexibility of one or both competent authorities is restricted. This is a matter for the competent authorities to determine on a case by case basis.

20. When deciding whether a MAP APA is appropriate, a key consideration is the extent of the advantage to be gained by agreeing a method for avoiding the risk of double taxation in advance. This requires the exercise of judgement and the need to balance the efficient use of limited resources, both financial and human, with the desire to reduce the likelihood of double taxation. Tax administrations might consider the following items as relevant:

a) Does the methodology and the other terms and conditions of the proposal respect the guidance given by the Transfer Pricing Guidelines? If not, it will be desirable to get the taxpayer to revise the proposal accordingly, in order to increase the chances of reaching a mutual agreement. As paragraph 17 of the preface to the Transfer Pricing Guidelines states “These guidelines are also intended primarily to govern the resolution of transfer pricing cases in mutual agreement proceedings”.

b) Are any “difficulties or doubts as to the interpretation or application of the Convention” likely to significantly increase the risk of double taxation and so justify the use of resources to settle any problems in advance of the proposed transactions?

c) Would the transactions covered by the proposal be ongoing in nature and is there a significant part of any limited life project left?

d) Are the transactions in question seriously contemplated and not of a purely hypothetical nature? The process should not be used to find out the likely views of the tax administration on a general point of principle - there are other established methods for doing this in many countries.

e) Is a transfer pricing audit already in progress in relation to past years where the fact pattern was substantially similar? If so, the outcome of the audit may be expedited by participating in a MAP APA, the terms of which could then be applied to inform or resolve the audit and any unresolved mutual agreement for earlier years.

### iii) Multilateral MAP APAs

21. The desire for certainty has resulted in an emerging trend for taxpayers to seek multilateral MAP APAs covering their global operations. The taxpayer approaches each of the affected jurisdictions with an overall proposal and suggests that it would be desirable if the negotiations be conducted on a multilateral basis involving all the affected jurisdictions, rather than by a series of separate negotiations with each tax authority. It should be noted that there is no multilateral method of implementing any agreement that may be reached, except by concluding a series of separate bilateral MAP APAs. The successful negotiation of a series of bilateral MAP APAs in this way would provide greater certainty and lower costs to the MNE group than if separate MAP APAs were undertaken bilaterally and in isolation of each other.

22. Although, as described above, there are potential benefits to having multilateral MAP APAs, a number of issues need to be considered. First, it is unlikely to be appropriate for a single transfer pricing methodology to be applied to the wide variety of facts and circumstances, transactions and countries likely to be the subject of a multilateral MAP APA, unless the methodology can be appropriately adapted to reflect the particular facts and circumstances found in each country. Therefore, care would need to be taken by all the participating jurisdictions to ensure that the methodology, even after such adaptation, represented a proper application of the arm’s length principle in the conditions found in their country.

23. Second, issues also arise because under a multilateral MAP APA several competent authorities are effectively involved in a process that was designed for a bilateral process. One issue is the extent to which it may be necessary to exchange information between all the affected jurisdictions. This could be problematic in cases where there are no transaction flows or common transactions between two or more of the affected treaty partners, so creating doubts as to whether the information is relevant to the particular bilateral MAP APA being discussed. However, in cases where similar transactions are conducted by different parts of the MNE or in which the area considered relates to trading on an integrated basis, there may be a need to have information about flows between other parties in order to be able to understand and evaluate the flows that are the subject of the particular bilateral MAP APA. Another problem is that it may be difficult to judge whether such information is indeed relevant prior to obtaining it.

24. Further, even if the information is relevant to the particular bilateral MAP APA, there may still be potential problems of confidentiality preventing the exchange of that information, either under the terms of the Exchange of Information Article(s) of the relevant treaty or under the domestic law of one of the participating tax administrations. Given the wide range of possible circumstances likely to be found in multilateral MAP APAs, no general solution to these problems can be prescribed. Rather such issues need to be addressed specifically in each of the separate bilateral MAP APAs.

25. In cases where information about flows between other parties is found to be relevant, some exchange of information problems could possibly be overcome by not relying on treaty information exchange provisions, but instead asking the taxpayer to assume responsibility for providing information to all the affected tax administrations (though procedures would still be needed to verify that the same information is in fact provided to all tax administrations). Finally, in some cases the mutual agreement articles of the relevant treaties may not provide an adequate basis for such multilateral consideration and discussion, although the Mutual Agreement Article of the OECD Model Tax Convention is designed to assist in the elimination of double taxation in a wide variety of circumstances, and therefore would, if applicable, appear to provide adequate authority in most situations.

26. In summary, as discussed in part A of this section, the desire by the taxpayer for certainty is not by itself sufficient to oblige a tax administration to enter into a MAP APA where this might be inappropriate. An invitation to participate in a multilateral MAP APA would therefore be evaluated in accordance with the usual criteria for determining whether a bilateral MAP APA could be pursued and each proposed bilateral APA would also be separately evaluated. A decision would then be taken whether the completion of the negotiations for the bilateral MAP APAs that the administration has decided to pursue, would best be served by its participation in multilateral negotiations. This evaluation will be made on a case-by-case basis.

27. The development of multilateral MAP APAs is at a relatively early stage, except perhaps in the global trading field. Indeed, where global trading is conducted on a fully integrated basis (i.e. the trading and risk management of a book of financial products takes place in a number of different locations, usually at least three), a multilateral, as opposed to a bilateral, APA has become the norm<sup>3</sup>. It is intended to monitor closely further developments in the area of multilateral MAP APAs.

### C. REQUESTS FOR MAP APAs

#### i) Introduction

28. Although a MAP APA by its nature involves an agreement between tax administrations, the process needs considerable involvement by the taxpayer or taxpayers in order to be successful. This section looks at the first stages in this process, namely the request for the MAP APA which is normally initiated by the taxpayer(s). (N.B. Some tax administrations consider that they should take the initiative and actively encourage taxpayers to make requests in appropriate cases, for example following completion of an audit or risk assessment analysis.) Once it has been decided that a MAP APA is indeed appropriate, the primary responsibility for providing the participating tax administrations with sufficient information for them to be able to conduct mutual agreement negotiations will inevitably rest with the taxpayer(s). Consequently, the taxpayer should submit a detailed proposal for review by the relevant tax administration and be prepared to provide further information as requested by the tax administration.

#### ii) Preliminary discussions

29. A feature of many domestic procedures for the obtaining of a unilateral APA is the ability to have a preliminary meeting (or meetings) before a formal request is made. Such a meeting (or meetings) provides a taxpayer with an opportunity to discuss with the tax administration the suitability of an APA, the type and extent of information which may be required and the scope of any analyses required for the completion of a successful APA. (For example: the extent of any functional analysis of affiliated enterprises; identification, selection and adjustment of comparables; and the need for, and the scope of, market, industry and geographic analyses.) The process also provides the taxpayer with an opportunity to

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<sup>3</sup> For more details see OECD Document: The Taxation of Global Trading of Financial Instruments (1998)

discuss any concerns regarding disclosure and confidentiality of data, the term of the APA and the like. Experience has generally shown that the ability to have such preliminary discussions expedites the processing of any subsequent formal MAP APA proposal.

30. In the context of a MAP APA, the ability of the relevant competent authorities to have preliminary discussions with the taxpayer(s) may also be useful. In addition to the matters mentioned above, the discussions could usefully explore whether the circumstances were suitable for a MAP APA, for example whether there were sufficient “difficulties or doubts as to the interpretation or application of the Convention”.

31. The preliminary meeting may also have a useful role in clarifying the expectations and objectives of the taxpayer(s) and the tax administration. It also provides an opportunity to explain the process, the policy of the tax administration on MAP APAs and to give details of any procedures for giving effect in domestic law to the agreement when completed. At the same time, the tax administration could provide guidance as to the content of the proposal, and the time frame for evaluating and concluding the mutual agreement. Tax administrations should publish general guidance on the MAP APA process in accordance with the recommendation for other types of mutual agreements at paragraphs 4.61-4.62 of the Transfer Pricing Guidelines.

32. The preliminary meeting process may be conducted on either an anonymous or a named basis, depending on domestic custom and practice. If on an anonymous basis, however, sufficient information about the operations will be required in order to make any discussion meaningful. The form of any meetings should be agreed between the parties and a preliminary meeting may range from a n informal discussion to a formal presentation. Typically, it is in the taxpayer’s interest to provide the tax administration with a memorandum outlining the topics for discussion. More than one preliminary meeting may be required in order to achieve the objective of having an informal discussion of the potential suitability of a MAP APA request, its likely scope, the appropriateness of a methodology or the type and extent of information to be provided by the taxpayer.

33. As well as informal discussions with its taxpayer(s), it may be useful for the respective competent authorities to have an early exchange of views on whether a MAP APA would be appropriate. This could avoid unnecessary work if it is unlikely that one of the competent authorities will participate. These discussions may be of an informal nature and do not necessarily require a formal face to face meeting. Also there may be opportunities to have such exchanges during the course of regular competent authority meetings and negotiations.

### iii) MAP APA Proposals

#### a) Introduction

34. If the taxpayer wishes to pursue a MAP APA request, it will need to make a detailed proposal to the relevant tax administration, pursuant to any domestic procedural requirements, e.g. a requirement to file the request with a designated part of the domestic tax administration. For a MAP APA, the purpose of the taxpayer’s proposal is to give the relevant competent authorities all the information needed to evaluate the proposal and to undertake mutual agreement discussions. Countries have a number of ways of ensuring the competent authorities get the necessary information. One way is for the taxpayer to be able to make the proposal directly to the competent authority. Another way of achieving this goal is for the taxpayer to make available a copy of any domestic APA proposal to the other participating jurisdictions. Ideally, the exact form and content of the proposal will have been established at any preliminary meetings.

#### b) Activities usually covered in a MAP APA process

35. The scope of the MAP APA would depend on the wishes of the participating jurisdictions, as well as those of the taxpayer. It can apply to resolve issues covered by Articles 7 and 9 of the OECD Model Convention and would determine to what extents profits would arise in the tax jurisdictions involved.

36. The MAP APA may cover all of the transfer pricing issues of a taxpayer (or of the members of a MNE group) or may be more limited, for example to a particular transaction, sets of transactions, product lines or to only some members of a MNE group. Some countries, whilst recognising the need for flexibility in the process, have concerns over the appropriateness of specific issue APAs. It may be difficult to evaluate some issues in isolation, for example where the transactions covered by the proposal are highly interrelated with transactions not covered by the proposal, or where there is a need to analyse transfer pricing issues in a wider context because intentional set offs are involved (see paragraphs 1.60 -1.64 of the Transfer Pricing Guidelines).

37. A MAP APA may also cover issues other than the transfer pricing methodology, provided that these other issues are sufficiently clearly connected to the underlying transfer pricing issues so as to make it worthwhile attempting to resolve them in advance and provided that the other issues come within the terms of the Mutual Agreement Article in the relevant treaty. That will be something to be decided between the affected parties for each individual case.

#### c) Content of a MAP APA proposal

38. The content of the proposal and the extent of the necessary supporting information and documentation will depend on the facts and circumstances of each case and the requirements of the individual participating tax administrations. It is therefore not considered practicable to list or define exactly what should be provided. The guiding principle, however, should be to provide the information and documentation necessary to explain the facts relevant to the proposed methodology and to demonstrate its application in accordance with the appropriate Article of the relevant treaty. The proposal should therefore be consistent with any general guidance given by the Commentary of the OECD Model Tax Convention on the corresponding Articles, together with the guidance on the application of the arm's length principle of Article 9 given by the Transfer Pricing Guidelines in cases involving transfer pricing between associated enterprises.

39. In terms of the supporting information and documentation to be included, the guidance in Chapter IV (paragraphs 4.155-158) and Chapter V of the Transfer Pricing Guidelines on documentation requirements should be borne in mind. However, because of the prospective nature of the agreement sought, different types of information may need to be supplied than in mutual agreement cases, which only relate to transactions already undertaken. As a guide, the following information may be of general relevance for MAP APAs, although it should be stressed that the list below is not intended to be exhaustive or prescriptive in nature:

a) the transactions, products, businesses or arrangements that will be covered by the proposal; (including, if applicable, a brief explanation of why not all of the transactions, products, businesses or arrangements of the taxpayer(s) involved in the request have been included);

b) the enterprises and permanent establishments involved in these transactions or arrangements;

c) the other country or countries which have been requested to participate;

d) information regarding the world-wide organisational structure, history, financial statement data, products, functions and assets (tangible and intangible) of any associated enterprises involved;

- e) a description of the proposed transfer pricing methodology and details of information and analyses supporting that methodology, e.g. identification of comparable prices or margins and expected range of results etc.;
- f) the assumptions underpinning the proposal and a discussion of the effect of changes in those assumptions or other events, such as unexpected results, which might affect the continuing validity of the proposal;
- g) the accounting periods or tax years to be covered;
- h) general description of market conditions (e.g. industry trends and the competitive environment);
- i) a discussion of any pertinent ancillary tax issues raised by the proposed methodology;
- j) a discussion of, and demonstration of compliance with, any pertinent domestic law, tax treaty provisions and OECD guidelines that relate to the proposal; and
- k) any other information which may have a bearing on the current or proposed transfer pricing methodology and the underlying data for any party to the request.

The rest of this section discusses some of the most important items from the above list in more detail.

#### d) Comparable pricing information

40. The taxpayer should include a discussion of the availability and use of comparable pricing information. This would include a description of how the search for comparables was carried out (including search criteria employed), what data relating to uncontrolled transactions was obtained and how such data was accepted or rejected as being comparable. The taxpayer should also include a presentation of comparable transactions along with adjustments to account for material differences, if any, between controlled and uncontrolled transactions. In cases where no comparables can be identified, the taxpayer should demonstrate, by reference to relevant market and financial data (including the internal data of the taxpayer), how the chosen methodology accurately reflects the arm's length principle.

#### e) Methodology

41. The MAP APA proposal should provide a full description of the chosen methodology. In cases involving associated enterprises, the chosen methodology should also respect the guidance found in the Transfer Pricing Guidelines on applying the arm's length principle of Article 9 of the OECD Model Tax Convention. It is stated at paragraph 1.70 of the Transfer Pricing Guidelines that "Further, any method should be permitted where its application is agreeable to the members of the MNE group involved with the transaction or transactions to which the methodology applies and also to the tax administrations in the jurisdictions of all those members." That guidance on use of transfer pricing methods is particularly relevant in the context of a MAP APA, because of the opportunity to obtain advance agreement on the method to be used. The application of the methodology should be supported by data which can be obtained and updated over the period of the MAP APA without imposing too great a burden on the taxpayer, and which can be reviewed and verified effectively by the tax administrations.

42. The taxpayer should, to the extent possible, provide an analysis of the effect of applying the chosen methodology or methodologies during the proposed period of the agreement. Such an analysis necessarily will have to be based on projected results and so details of the assumptions on which those projections were made will be needed. It may also be helpful to illustrate the effect of applying the APA methodology or methodologies to the periods immediately before the APA period. The usefulness of this analysis, even

as an illustration, will depend on the facts and circumstances surrounding the transactions in question being comparable to those applying to the prospective transactions contemplated under the proposal.

f) Critical assumptions

43. In entering into a MAP APA relating to the arm's length pricing of controlled transactions that have not yet occurred, it is necessary to make certain assumptions about the operational and economic conditions that will affect those transactions when they take place. The taxpayer should describe in the proposal the assumptions on which the ability of the methodology to accurately reflect the arm's length pricing of future transactions is based. Additionally, the taxpayer should explain how the chosen methodology will satisfactorily cope with any changes in those assumptions. The assumptions are defined as "critical" if the actual conditions existing at the time the transactions occur could diverge from those that were assumed to exist, to the extent that the ability of the methodology reliably to reflect arm's length pricing is undermined. One example might be a fundamental change to the market arising from new technology, government regulations, or widespread loss of consumer acceptance. In such a case, the divergence may mean that the agreement would need to be revised or cancelled.

44. To increase the reliability of the MAP APA methodology, taxpayers and tax administrations should attempt to identify critical assumptions that are, where possible, based on observable, reliable and independent data. Such assumptions are not limited to items within the control of the taxpayer. Any set of critical assumptions needs to be tailored to the individual circumstances of the taxpayer, the particular commercial environment, the methodology, and the type of transactions covered. They should not be drawn so tightly that certainty provided by the agreement is jeopardised, but should encompass as wide a range of variation in the underlying facts as the parties to the agreement feel comfortable with. In general, however, and by way of example only, critical assumptions might include:

- a) assumptions about the relevant domestic tax law and treaty provisions;
- b) assumptions about tariffs, duties, import restrictions and government regulations;
- c) assumptions about economic conditions, market share, market conditions, end-selling price, and sales volume;
- d) assumptions about the nature of the functions and risks of the enterprises involved in the transactions;
- e) assumptions about exchange rates, interest rates, credit rating and capital structure;
- f) assumptions about management or financial accounting and classification of income and expenses; and
- g) assumptions about the enterprises that will operate in each jurisdiction and the form in which they will do so.

45. It may also be helpful to set parameters for an acceptable level of divergence for some assumptions in advance, in order to provide the necessary flexibility. These parameters would need to be set individually for each particular MAP APA and would form part of the negotiations between the competent authorities. Only if the divergence from the prediction exceeded the parameter would the assumption become "critical" and action considered. Any action to be taken might also depend on the nature of the assumption and the level of divergence.

46. If the reliability of the proposed transfer pricing methodology is known to be sensitive to exchange rate fluctuations, it would seem sensible to design a methodology that was capable of accommodating a certain degree of expected fluctuation, perhaps by providing for prices to be adjusted to take into account

exchange rate movements. Also it could be agreed in advance that movements in either direction of up to X% would require no action, that movements greater than X % but less than Y% would trigger a prospective review of the methodology to make sure it remained appropriate, whilst a movement of more than Y% would mean that a critical assumption had been breached and it would be necessary to prospectively re-negotiate the MAP APA. These parameters would need to be set individually for each particular MAP APA and would form part of the negotiation between the competent authorities.

#### g) Unexpected results

47. A problem may arise when the results of applying the transfer pricing methodology agreed in the MAP APA do not fulfil the expectations of one of the parties, as that party may question whether the critical assumptions, and the methodology which they support, are still valid. The resolution of such questions may take a considerable amount of time and effort, thereby negating one of the objectives of the whole process. One possible solution to this problem is to include enough flexibility in the proposal to cope with likely changes in the facts and circumstances so that unexpected results are less likely to occur so that there is less risk that the MAP APA agreement based upon the proposal will need to be renegotiated. The proposal must still, of course, conform to the arm's length principle.

48. One way of achieving the above objective is to design a methodology that appropriately takes into account likely changes in facts and circumstances; for example, some variation between projected and actual sales volume can be built in to the pricing methodology at the outset by including prospective price adjustment clauses or allowing pricing to vary with volume. The allowable level of deviation should be set by reference to what would have been accepted by independent parties.

49. Another possible way of achieving the objective of increasing certainty, is to agree an acceptable range of results from applying the method of the MAP APA. In order to conform with the arm's length principle, the range should be agreed by all affected parties in advance, thereby avoiding the use of hindsight, and based on what independent parties would have agreed to in comparable circumstances (see paragraphs 1.45-1.48 for discussion of the range concept). For example, the quantum of an item, such as a royalty, would be accepted so long as it remained within a certain range expressed as a proportion of the profits.

50. If the results fall outside the agreed range, the action to be taken would depend on what had been negotiated in the proposal in accordance with the wishes of the parties. Some parties may not wish to take the risk that the results will be significantly different from what they expected. Accordingly, they would use the range concept simply as a means of determining whether a critical assumption had been breached as described in paragraph 46. Other parties may place more emphasis on certainty of treatment than on avoiding unexpected results and so may agree that the MAP APA should contain a mechanism for adjusting the results so that they fall within the range agreed in advance.

#### h) Duration of the MAP APA

51. By its nature, an APA applies to prospective transactions and so one issue to be decided is how long it will last. There are two sets of conflicting objectives that affect the negotiation of the appropriate term. On the one hand, it is desirable to have a sufficiently long period so as to grant a reasonable degree of certainty of treatment. Otherwise, it may not be worth making the initial effort of resolving potential transfer pricing problems in advance, as opposed to tackling problems only when they arise through the normal audit or tax return examination procedures. On the other hand, a long period makes the predictions as to future conditions on which the mutual agreement negotiations are based less accurate, thereby casting doubt on the reliability of the MAP APA proposals. The optimal trade-off between these two sets of objectives will depend on a number of factors, such as the industry, the transactions involved and the



economic climate. The term should therefore be negotiated between the competent authorities on a case-by-case basis. Experience to date has shown that a MAP APA might, on average, last for 3-5 years.

#### D. Finalisation of the MAP APA

##### i) Introduction

52. The success of the MAP APA process, as an alternative to relying solely on traditional audit or examination techniques, depends to a large extent on the commitment of all the participants. The ability of the relevant competent authorities to reach agreement in a prompt manner will be determined both by their actions and importantly by the willingness of the taxpayer(s) to provide all the necessary information as promptly as possible. The usefulness of the process, both for taxpayers and tax authorities, will be significantly diminished if the MAP APA is not agreed until the period proposed to be covered in the taxpayer's request has nearly expired. Such delay may also make it more difficult to avoid the use of hindsight when evaluating the proposal because the results of applying the methodology will be known for most of the period proposed by the MAP APA. Understandably, given the relatively early stage in the evolution of the MAP APA process, the goal of prompt prospective resolution has not always been met in the past. To some extent, of course, some delay in the process is inevitable; MAP APAs tend to deal with large taxpayers, complex fact patterns, and difficult legal and economic issues, all of which require time and resources in order to understand and evaluate.

53. Tax authorities are encouraged, where possible, to devote sufficient resources and skilled personnel to the process to ensure that cases are settled promptly and efficiently. Some tax authorities may wish to improve the efficiency of their MAP APA programmes by setting informal goals for the length of time taken to complete the process and by publishing the average completion time. Particular treaty partners may also agree to set informal goals for completion of their bilateral negotiations. Given the often complex and difficult fact patterns, the possible need for translations and the relative novelty of such arrangements, it is not felt desirable to set more specific or binding targets for concluding MAP APAs at this stage. However, it will be appropriate to set more specific targets for completion time in the future, once more experience with the MAP APA process has been gained.

54. Once a taxpayer's proposal has been received by the tax administrations, they should mutually agree on the co-ordination of the review, evaluation and negotiation of the MAP APA. The MAP APA process can conveniently be broken up into two main stages; (1) fact finding, review and evaluation and (2) the competent authority discussions, each of which is discussed in further detail below.

##### ii) Fact Finding, Review and Evaluation

###### a) General

55. In reviewing the MAP APA proposal, the tax administrations may undertake whatever steps they deem appropriate in the circumstances to conduct the Mutual Agreement process. These include, but are not limited to: requests for further information deemed relevant to review and evaluate the taxpayer's proposal, the carrying out of fieldwork (e.g. visits to taxpayer's premises, interviews with staff, review of financial or managerial operations, etc.) and the engaging of necessary experts. Tax administrations may also have recourse to information collected from other sources, including information and data on comparable taxpayers.

56. The aim of this stage of the MAP APA process is for the participating competent authorities to have all relevant information, data, and analyses they need for the negotiations. Where one tax administration obtains additional information from the taxpayer relevant to the subject of the MAP APA, for example at a meeting with the taxpayer's staff, both the taxpayer and the tax administration should ensure the

information reaches the other participating tax administration(s). The relevant competent authorities should arrange, amongst themselves and the taxpayers, for an appropriate mechanism to corroborate the completeness and details of documents and information supplied by the taxpayer(s). The requirements of the participating competent authorities should be respected. For example, many jurisdictions require that not only is the same factual information provided to all participating competent authorities but that it should, as far as is practicable, be made available at the same time.

57. The prospective nature of a MAP APA often involves the provision by the taxpayer of commercial information relating to forecasts which is likely to be even more sensitive to disclosure than information supplied after the event. Accordingly, in order to ensure that taxpayers have confidence in the MAP APA process, tax administrations should ensure that taxpayer information provided during the course of the MAP APA process is subject to the same secrecy, confidentiality and privacy safeguards of the relevant domestic law as any other taxpayer information. Further, where information is exchanged between competent authorities under the terms of the tax treaty, that information can be disclosed only in accordance with the specified terms of the treaty, and any exchange must comply with the Exchange of Information Article(s) of the relevant treaty.

58. Generally, the competent authorities would conduct simultaneous, independent reviews and evaluations of the taxpayer's proposal, assisted in this task, where necessary, by transfer pricing, industry, or other specialists from elsewhere in their tax administration. However, it may be more efficient in appropriate cases to have some degree of joint fact finding. This could take a variety of forms ranging from an occasional joint fact finding meeting or site visit, to the preparation of a joint report by delegated caseworkers as outlined at paragraph 4.55 of the Transfer Pricing Guidelines.

#### b) Role of taxpayer in the fact finding, review and evaluation process

59. In order to expedite the process, taxpayers should take responsibility for ensuring that the competent authorities, before they start to negotiate, are in possession of the same facts, have all the information they need and have a thorough understanding of the issues. This can be achieved by the taxpayer routinely making information requested by one tax administration available, at broadly the same time, to the other tax administration, preparing and transmitting notes of fact finding meetings by one tax administration to the other tax administration and where logistically and economically practical, facilitating joint fact finding meetings. The taxpayer should also arrange for any necessary translations to be made and ensure there is no undue delay in responding to requests for further relevant information. The taxpayer should also be entitled to confer with its tax administrations when mutually appropriate and convenient while the proposal is undergoing review and evaluation, and should be kept informed of progress.

#### iii) Conduct of Competent Authority discussions

##### a) Co-ordination amongst the Competent Authorities

60. Many countries prefer to be fully involved in the process as soon as it commences and wish to work closely with the other competent authorities.

Other countries prefer to confine their involvement to reviewing and commenting upon the MAP APA proposals as they near completion. However, the involvement of all participating tax administrations in the process at an early stage is recommended, subject to resource constraints, as this should maximise the efficiency of the process and help forestall unnecessary delays in concluding the mutual agreement.

61. The competent authorities should conduct the mutual agreement discussions in a timely manner. This requires the devotion of sufficient resources and appropriately skilled personnel to the process. It is desirable that the competent authorities discuss and co-ordinate an appropriate plan of action with regards to such matters as: designating authorised officers, exchanging of information, co-ordination of the review

and evaluation of the proposal, tentative scheduling of dates for further consultations, negotiation and conclusion of a suitable agreement. The level of input and resources required should be tailored to the individual requirements of the case.

62. Experience has also shown that early and frequent discussion between the competent authorities as problems arise can be helpful and can avoid unpleasant surprises during the process. Given the nature of MAP APAs, there will often be significant issues which cannot be resolved simply by exchange of position papers and so more formal exchanges, such as face to face meetings between the competent authorities may be required. Use of conference calls or video conferencing may be helpful.

b) Role of the taxpayer in Competent Authority discussions

63. The role of the taxpayer in this process is necessarily more limited, than in the fact finding process, given that the finalisation of a MAP APA is a government to government process. The competent authorities may agree to have the taxpayer make a presentation of the factual and legal issues before the discussions themselves commence, when the taxpayer would leave. It also may be helpful to arrange to have the taxpayer available, on call, to answer any factual questions that may arise during the discussions. The taxpayer should avoid presenting new factual information or making supplementary representations at this meeting. The tax authorities will require time to review such matters and this will necessitate a postponement of a final decision on the proposed MAP APA. Such information should have been supplied prior to the commencement of the discussions.

c) Withdrawal from the APA process

64. The taxpayer or tax administration may withdraw from the MAP APA process at any time. However, withdrawal from the process, especially at a late stage and without good cause, should be discouraged because of the inevitable waste of resources caused by such action. When a MAP APA request is withdrawn neither the taxpayer nor the tax administrations should have any obligations to each other, and any previous undertakings and understandings between the parties would be of no further force and effect, unless otherwise required by domestic law (e.g. APA user fee may not be refundable). If a tax administration proposes to withdraw, the taxpayer should be advised of the reasons for such action and given an opportunity to make further representations.

d) Mutual Agreement document

65. Participating competent authorities should prepare a draft mutual agreement when they have agreed on the methodology and other terms and conditions. It may be that, despite the best efforts of the competent authorities, the proposed mutual agreement does not completely eliminate double taxation. The taxpayer(s) should therefore be given an opportunity to say whether such a draft MAP APA is acceptable before it is finalised; there can be no question of imposing such an agreement in advance without the taxpayer's consent.

66. The MAP APA will be in the form of a written document and the content, layout etc. will be decided by the participating competent authorities. In order to achieve the objective of providing a clear record of the mutual agreement and for the agreement to be effectively implemented, the mutual agreement should contain the following minimum information or should refer to where this information is provided in the MAP APA proposal documentation:

a) the names and addresses of the enterprises that are covered by the arrangement;

b) the transactions, agreements or arrangements, tax years or accounting periods covered;

- c) a description of the agreed methodology and other related matters such as agreed comparables or a range of expected results;
- d) a definition of relevant terms which form the basis of applying and calculating the methodology (e.g., sales, cost of sales, gross profit, etc.);
- e) critical assumptions upon which the methodology is based, the breach of which would trigger renegotiation of the agreement;
- f) any agreed procedures to deal with changes in the factual circumstances which fall short of necessitating the renegotiation of the agreement;
- g) if applicable, the agreed tax treatment of ancillary issues;
- h) the terms and conditions that must be fulfilled by the taxpayer in order for the mutual agreement to remain valid together with procedures to ensure that the taxpayer is fulfilling those terms and conditions;
- i) details of the taxpayer's obligations to the tax administrations as a result of the domestic implementation of the MAP APA (e.g., annual reports, record keeping, notification of changes in critical assumptions etc.); and
- j) confirmation that, in order to secure the confidence of taxpayers and competent authorities in a MAP APA process in which information is exchanged freely, all information submitted by a taxpayer in a MAP APA case (including the identity of the taxpayer) will be protected from disclosure to the fullest extent possible under the domestic laws of the respective jurisdictions and all information exchanged between the competent authorities involved in such a case will be protected in accordance with the relevant bilateral tax treaty and applicable domestic laws.

#### iv) Implementation of the MAP APA

##### a) Giving effect to the MAP APA and providing confirmation to the taxpayer

67. Once the MAP APA has been finally agreed, the participating tax authorities need to give effect to the agreement in their own jurisdiction. The tax administrations should enter into some kind of a confirmation or agreement with their respective taxpayers consistent with the mutual agreement entered into by the participating competent authorities. This confirmation or agreement would provide the taxpayer with the certainty that the transfer pricing transactions covered by the MAP APA would not be adjusted, so long as the taxpayer complies with the terms and conditions of the mutual agreement, as reflected in the domestic confirmation or agreement and has not made materially false or misleading statements during the process, including statements made in annual compliance reports. The terms and conditions would include certain assumptions which, if not met, might require an adjustment to be made or the agreement to be reconsidered.

68. The way this confirmation or agreement is given will vary from country to country and the exact form will depend on the particular domestic law and practice. In some countries the confirmation or agreement will take the form of an APA under the relevant domestic procedure. To implement the mutual agreement effectively, the domestic confirmation or agreement must be consistent with the MAP APA and give the taxpayer, as a minimum, the same benefits as negotiated in the mutual agreement. Additionally, where it was not possible to completely eliminate double taxation, it is open to one of the participating jurisdictions to give unilateral relief from the remaining double taxation in its domestic confirmation procedure. Also, that confirmation or agreement may cover additional matters to those contained in the MAP APA, for example the domestic tax treatment of other or ancillary issues, additional record keeping

or documentation requirements and the filing of reports. Care should be taken to ensure that none of the additional terms of the domestic confirmation or agreement conflict with the terms of the MAP APA.

b) Possible retroactive application (“Roll back”)

69. Neither the tax administrations nor the taxpayer are in any way obliged to apply the methodology agreed upon as part of the MAP APA to tax years ending prior to the first year of the MAP APA (often referred to as “rolling back”). Indeed, to do so might be impossible if a different fact pattern then prevailed. However, the methodology to be applied prospectively under the MAP APA may be instructive in determining the treatment of comparable transactions in earlier years. In some cases, the transfer prices may already be under enquiry by one tax administration in accounting periods prior to the MAP APA period and that tax administration and the taxpayer may wish to take the opportunity to use the agreed methodology to resolve the enquiry, or, pursuant to domestic law requirements, the tax administration may choose to make such an adjustment even without the taxpayer’s request or agreement. If the taxpayer wants certainty of obtaining relief from double taxation, the consent of the other affected tax administration(s) to the “roll back” would be needed. The ability to “roll back” will also depend on the relevant domestic law and the treaty, for example with regard to time limits.

E. MAP APA Monitoring

70. It is essential that the tax administrations are able to establish that the taxpayer is abiding by the terms and conditions on which the mutual agreement is based, throughout its duration. As the mutual agreement is made between the tax administrations and the taxpayer is not a party to such arrangements, the tax administrations have to rely on the domestic confirmation or agreement procedure described above in order to monitor the taxpayer’s compliance. If the taxpayer fails to abide by the terms and conditions of the MAP APA, then it no longer need be applied. This section therefore focuses on the aspects of the domestic procedures necessary for the successful implementation of the MAP APA and on the necessary measures to ensure the taxpayer’s compliance with all of its terms and conditions.

i) Record keeping

71. The taxpayer and the tax administrations should agree the types of documents and records (including any necessary translations) that the taxpayer must maintain and retain for the purposes of verifying the extent of the taxpayer’s compliance with the MAP APA. The guidance in Chapters IV and V of the Transfer Pricing Guidelines should be followed in order to avoid the documentation requirements becoming overly burdensome. Provisions regarding the retention period and the response time for producing the documents and records may also be included.

ii) Monitoring mechanisms

a) Annual reports

72. For each tax year, or accounting period, covered by the MAP APA, the taxpayer may be required to file, in addition to its tax return, an annual report describing the taxpayer's actual operations for the year and demonstrating compliance with the terms and conditions of the MAP APA, including the information necessary to decide if the critical assumptions, or other safeguards, have been met. This information should be made available by the taxpayer to the tax administration with which it has concluded the domestic confirmation or agreement, in the manner provided for under the relevant domestic law or procedure.

b) Audit

73. A MAP APA applies only to the parties specified in the agreement and in respect of the specified transactions. The existence of such an agreement would not prevent the participating tax administrations from undertaking audit activity in the future, although any audit of transactions that are covered by the MAP APA would be limited to determining the extent of the taxpayer's compliance with its terms and conditions and whether the circumstances and assumptions necessary for the reliable application of the chosen methodology continue to exist. The affected tax administrations may require the taxpayer to establish that:

- a) the taxpayer has complied with the terms and conditions of the MAP APA;
- b) the representations in the proposal, the annual reports and in any supporting documentation, remain valid and that any material changes in facts or circumstances have been included in the annual reports;
- c) the methodology has been accurately and consistently applied in accordance with the terms and conditions of the MAP APA; and
- d) the critical assumptions underlying the transfer pricing methodology remain valid.

iii) Consequences of non compliance or changes in circumstances

74. In general, the consequences of non compliance with the terms and conditions of a MAP APA, or the failure to meet a critical assumption, will turn on (i) the terms of the MAP APA, (ii) any further agreement between the competent authorities as to how to deal with such non compliance or failure, and (iii) any applicable domestic law or procedural provisions. That is, the MAP APA itself may explicitly prescribe procedures to follow, or describe the consequences that will arise, in situations of non compliance or failure. In such situations, the competent authorities may, at their discretion, enter into discussions of what action to take on a case by case basis. Finally, domestic law or procedural provisions may impose consequences or obligations on the taxpayer and affected tax administration. The following paragraphs provide suggested guidelines similar to procedures that have been adopted in some jurisdictions and which have, on the whole, proved workable. It should be emphasised, however, that some tax administrations may wish to adopt different procedures and approaches.

75. If the tax administrations determine that any requirement of the MAP APA has not been met, they may nevertheless agree, based on the terms and conditions of the MAP APA, to continue to apply it, for example where the effect of the failure to comply is not material. If they do not agree to continue to apply the MAP APA, there are three options that a tax administration could take. The nature of the action to be taken is likely to depend on the seriousness of the non compliance.

76. The most drastic action is revocation, which has the effect that the taxpayer is treated as if the MAP APA had never been entered into. Less serious is cancellation, which means the taxpayer is treated as if the MAP APA had been effective and in force but only up to the cancellation date and not for the whole of the proposed period. If the MAP APA is cancelled or revoked, then for those tax years or accounting periods for which the cancellation or revocation is effective, the relevant tax administrations and taxpayers will retain all their rights under their domestic laws and treaty provisions, as though the MAP APA had not been undertaken. Finally, the MAP APA may be revised, which means that the taxpayer will still have the benefit of the MAP APA for the whole of the proposed period, albeit that different terms apply before and after the revision date. Further details are provided below.

a) Revoking a MAP APA

77. A tax administration may revoke a MAP APA (either unilaterally or by mutual agreement) if it is established that:

a) there was a misrepresentation, mistake or omission that was attributable to the neglect, carelessness, or wilful default of a taxpayer when filing the MAP APA request and submission, the annual reports, or other supporting documentation or in supplying any related information; or

b) the participating taxpayer(s) failed to materially comply with a fundamental term or condition of the MAP APA.

78. When a MAP APA is revoked, the revocation is retroactive to the first day of the first tax year or accounting period for which the MAP APA was effective and the MAP APA will no longer have any further force and effect on the affected taxpayer(s) and the other tax administration. Because of the serious effect of this action, the tax administration proposing to revoke a MAP APA should only do so after a careful and thorough evaluation of the relevant facts and should inform and consult with the affected taxpayer(s) and other tax administration(s) on a timely basis.

b) Cancelling a MAP APA

79. A tax administration may cancel a MAP APA (either unilaterally or by mutual agreement) if it is established that one of the following situations has arisen:

a) there was a misrepresentation, mistake or omission that was not attributable to the neglect, carelessness, or wilful default of a taxpayer when filing the MAP APA request and submission, the annual reports, or other supporting documentation or in supplying any related information; or

b) the participating taxpayer(s) failed to materially comply with any term or condition of the MAP APA; or

c) there was a material breach of one or more of the critical assumptions; or

d) there was a change in tax law, including a treaty provision materially relevant to the MAP APA; and it has not proved possible to revise the agreement (see paragraphs 80-82 below) to take account of the changed circumstances.

80. When a MAP APA is cancelled the date of cancellation will be determined by the nature of the event that led to the cancellation. This may be a specific date, for example if the event giving rise to the cancellation was a material change in tax law (although the MAP APA may still provide for there to be a period of transition between the date of change in the law and the cancellation date). In other cases, the cancellation will be effective for a particular tax year or accounting period, for example where there was a material change in one of the critical assumptions which could not be ascribed to a particular date in that tax year or accounting period. The MAP APA will no longer have any further force on the affected taxpayer(s) and the other tax administration from the date of cancellation.

81. The tax administration may waive cancellation if the taxpayer can show reasonable cause, to the satisfaction of the tax administration, and if the taxpayer agrees to make any adjustment proposed by the tax administration to correct the misrepresentation, mistake, omission or non-compliance, or take into account the changes in critical assumptions, tax law or treaty provision relevant to the APA. Such action may give rise to the revision of the MAP APA (see below).

82. The tax administration proposing the cancellation should inform and consult with the affected taxpayer(s) and the other tax administration(s) in a timely manner. This consultation should include an explanation of the reasons for proposing that the APA be cancelled. The taxpayer should be given an opportunity to respond before any final decision is taken.

#### c) Revising a MAP APA

83. The validity of the transfer pricing methodology is dependent on the critical assumptions continuing to apply for the duration of the MAP APA. The MAP APA and any domestic confirmation or agreement should therefore require the taxpayer to notify the affected tax administrations of any changes. If, after evaluation by the tax administrations, it is established that there has been a material change in conditions noted in a critical assumption, the MAP APA may be revised to reflect the change. As discussed above, the MAP APA may also contain assumptions, which although falling short of being critical to the validity of the MAP APA, nevertheless warrant a review by the affected parties. One result of such a review may again be a revision of the MAP APA. However, in many cases the terms and conditions of the MAP APA may be sufficiently flexible to account for the effects of such changes without the need for revision.

84. The taxpayer's notification to the tax administrations that such a change has taken place should be filed as soon as practicable after the change occurs, or the taxpayer becomes aware of the change, and in any event no later than the date for filing, if required, the annual report for that year or accounting period. Early notification is encouraged in order to give the affected parties more time to try to reach agreement on revising the MAP APA, thereby reducing the likelihood of cancellation.

85. The revised MAP APA should state the date from which the revision is effective and also the date on which the original MAP APA is no longer effective. If the date of the change can be precisely identified, then normally the revision should take effect from that date but if a precise date cannot be identified, then normally the MAP APA would be revised with effect from the first day of the accounting period following the one in which the change took place. If the tax administrations and the taxpayer cannot agree on the need for a revised MAP APA or how to revise the MAP APA, the MAP APA will be cancelled and will no longer have any further force and effect on the participating taxpayers and tax administrations. The determination of the effective date of the cancellation of the MAP APA will normally follow the same principles as applied to determine the date of revision.

#### iv) Renewing a MAP APA

86. A request to renew a MAP APA should be made at the time prescribed by the participating tax administrations, bearing in mind the need for sufficient lead time for the taxpayer(s) and tax administrations to review and evaluate the renewal request and to reach agreement. It may be helpful to commence the renewal process well before the existing MAP APA has expired.

87. The format, processing, and evaluation of the renewal application would usually be similar to those for an initial MAP APA application. However, the necessary level of detail may be reduced with the agreement of the participating tax administrations, particularly if there have not been material changes in the facts and circumstances of the case. Renewal of a MAP APA is not automatic and depends on the consent of all parties concerned and on the taxpayer demonstrating, among other things, compliance with the terms and conditions of the existing MAP APA. The methodology and terms and conditions of the renewed MAP APA may, of course, differ from those of the previous MAP APA.